

**UNITED STATES BANKRUPTCY COURT
DISTRICT OF NEW HAMPSHIRE**

In re:

Bk. No. 05-11004-JMD
Chapter 7

Kathy B. Mann,
Debtor

Edmond J. Ford, Chapter 7 Trustee,
Plaintiff

Adv. No. 05-01101-JMD

v.

Henry Blaine and
Gertrude Blaine,
Defendants

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MEMORANDUM OPINION

I. INTRODUCTION

Edmond Ford, Chapter 7 Trustee (the “Trustee”), commenced this adversary proceeding against the Debtor’s parents, Henry and Gertrude Blaine (the “Defendants”), seeking to set aside certain property transfers as fraudulent transfers pursuant to the New Hampshire Uniform Fraudulent Transfer Act, N.H. Rev. Stat. Ann. § 545-A (1997) (“NH RSA”) (“UFTA”) and 11

U.S.C. § 544.¹ The complaint was brought under two counts: Count I alleges that actual fraud was involved in a prepetition transfer by the Debtor to her parents under UFTA; Count II alleges the same actual fraud and that a lack of reasonably equivalent value was received by the Debtor for the same transfer.

A trial was held on December 13, 2005. At the beginning of the trial, the Trustee orally amended Count II to include constructive fraud under NH RSA 545-A:4(I)(b). At the close of the Trustee's case, the Defendants moved to dismiss. Finding that the Trustee failed to prove an actual intent to defraud, the Court granted the motion to dismiss as to Count I but denied it as to Count II. After the hearing, the Court took the case under advisement and the parties submitted post-trial memoranda.

This Court has jurisdiction of the subject matter and the parties pursuant to 28 U.S.C. §§ 1334 and 157(a) and the "Standing Order of Referral of Title 11 Proceedings to the United States Bankruptcy Court for the District of New Hampshire," dated January 18, 1994 (DiClerico, C.J.). This is a core proceeding in accordance with 28 U.S.C. § 157(b).

II. FACTS

The Trustee seeks to set aside a prepetition transfer made by the Debtor to the Defendants. The transfer consisted of a 3.8 acre parcel of real property (the "Parcel") that was contiguous with the Defendants' 62 acre homestead in Newport, New Hampshire.

¹ Unless otherwise indicated, all references to "section" or "§" refer to Title 11 of the United States Code, as in effect prior to the adoption of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8.

On or about April 12, 1999, the Defendants conveyed the Parcel to the Debtor for no consideration (the “1999 Conveyance”). The 1999 Conveyance was formalized with a warranty deed, which was recorded with the Sullivan County Registry of Deeds. Although nothing on the face of the deed indicates this was anything other than a standard conveyance of fee title, both the Debtor and her mother/co-defendant, Gertrude Blaine (“Debtor’s Mother”), testified that the conveyance was made with the understanding the Debtor and her husband would build a home on the Parcel so the Debtor could live close enough to her parents that she could care for them in their old age. No home was ever built on the Parcel.

Following the 1999 Conveyance, the Debtor and her husband separated and the Debtor began to experience financial difficulties. At some point thereafter, the Debtor received a delinquent tax notice indicating that \$1,015.54 was owed for real estate taxes on the Parcel for a portion of 2001 and 2002. Adjustments were made to the tax bill, and the adjusted amount was paid in full by a check signed by the Debtor’s Mother, drawn on the Defendants’ joint checking account on January 15, 2003.

On June 19, 2003, the Debtor took out a consolidation loan for \$11,227.00 with Lake Sunapee Bank (the “Sunapee Loan”). The Debtor testified that she did not qualify for the loan on her own so the Debtor’s Mother pledged the Defendants’ joint passbook savings account with Lake Sunapee Bank (the “Bank”) as security on the loan. The interest on the Sunapee Loan was set at 3.39%. The loan was in the Debtor’s name and executed by the Debtor, but the Debtor’s Mother signed the Third Party Agreement section of the loan and an Assignment of Deposit of Share Account on the same day. The Debtor’s Mother testified that she provided security on the Sunapee Loan so her daughter could get a low interest loan that would enable her to pay off her debts.

The Debtor testified that her intent in taking out the loan was to pay off her outstanding obligations. A credit report from the Credit Bureau of New Hampshire, prepared for the Bank the day before the Sunapee Loan was finalized, indicates that prior to the loan the Debtor had somewhere in the range of ten creditors. The Debtor testified that she retained 10% of the loan proceeds to cover living expenses for herself and her dependent child and used 90% of the loan proceeds to pay off existing creditors, leaving only two creditors—the Bank and Toyota Financial Services, the company holding the lease on her vehicle.

On July 1, 2003, the Debtor transferred the Parcel to the Defendants (the “2003 Conveyance”). As was the case with the 1999 Conveyance, the Defendants did not pay any consideration for the transfer. However, they took title to the property subject to outstanding real estate taxes. The 2003 Conveyance was formalized with a warranty deed recorded with the Sullivan County Registry of Deeds. The Debtor and the Debtor’s Mother testified that the transfer took place because the Debtor was not in a position to build a home on the property and it was a financial burden on the Debtor. They also testified that there was an understanding the property was meant to stay in the family if the Debtor did not build her home on it. Finally, the Debtor’s Mother testified that she and her husband do not intend to reconvey the Parcel to the Debtor in the future. The Debtor filed her bankruptcy petition on March 21, 2005, nearly one year and nine months after the 2003 Conveyance.

The Trustee alleges the Debtor fraudulently transferred the Parcel in violation of state fraudulent transfer laws, NH RSA 545-A:4, for which the Trustee seeks recovery of the Parcel. At the hearing, the Court determined the Trustee failed to prove actual fraud. Accordingly, the issue before the Court is whether or not the Trustee met the burden of proof for constructive fraud under UFTA.

III. DISCUSSION

A. New Hampshire Uniform Fraudulent Transfer Act (NH RSA 545-A)

1. Background

The Plaintiff brought his complaint under section 544(b) of the Bankruptcy Code seeking to avoid the transfer of the Parcel under UFTA, which provides in pertinent part:

A transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor's claim arose before or after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation:

- (a) With actual intent to hinder, delay, or defraud any creditor of the debtor; or
- (b) Without receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor:
 - (1) Was engaged or was about to engage in a business or a transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction; or
 - (2) Intended to incur, or believed or reasonably should have believed that he would incur, debts beyond his ability to pay as they became due.

NH RSA 545-A:4(I).

Under UFTA, transfers may be found to be fraudulent if made with actual intent to defraud ("actual" fraud)² or if made under circumstances that, in the absence of actual fraud, are deemed to be fraudulent ("constructive" fraud).³ At the trial, the Court determined that the Trustee had failed satisfy his burden of proof regarding actual fraud and dismissed Count I of the sComplaint. Accordingly, to prevail in this matter, the Trustee must prove constructive fraud under UFTA by a preponderance of the evidence. Dahar v. Jackson (In re Jackson), 318 B.R. 5, 13 (Bankr. D.N.H. 2004).

² NH RSA 545-A:4(I)(a).

³ NH RSA 545-A:4(I)(b).

UFTA requires creditors to prove two elements in order to prevail on a claim of constructive fraud:

1. The debtor transferred an asset or incurred a debt “without receiving a reasonably equivalent value in exchange for the transfer or obligation,”
2. “[A]nd the debtor” did either of the following:
 - a. “[W]as engaged or was about to engage in a business or a transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction; or”
 - b. “[I]ntended to incur, or believed or reasonably should have believed that he [or she] would incur, debts beyond his [or her] ability to pay as they became due.”

NH RSA 545-A:4(I)(b). The Court notes that the Debtor is not engaged in a business.

Accordingly, the Trustee’s claim for constructive fraud is limited to NH RSA 545-A:4(I)(b)(2).

a. Reasonably equivalent value.

The Trustee contends, and the Defendant does not dispute, that no consideration was paid for the transfer of the Parcel. Therefore, the first element of constructive fraud is established.

The Court notes, however, that although the parties apparently agree that the 2003 Conveyance was made for no consideration, a few months prior to the 2003 Conveyance, the Defendants paid \$1,010.71 in outstanding property taxes on behalf of the Debtor and took the Parcel subject to any remaining outstanding property taxes. Finally, the transfer occurred contemporaneously with the Defendants pledging their joint passbook savings account as security for the Debtor’s consolidation loan. Therefore, the 2003 Conveyance appears to be a part of a comprehensive plan by the Debtor and the Defendants to restructure the Debtor’s obligations outside of a bankruptcy proceeding. Accordingly, the Defendants’ assistance to the Debtor in that restructuring might constitute consideration paid by the Defendants for the 2003

Conveyance. Nonetheless, while no evidence was presented by any party on the value of the Parcel at the time of the 2003 Conveyance, it is undisputed that the value of any such consideration was less than the market value of the Parcel at the time of the 2003 Conveyance.

b. Incurring debts beyond an ability to pay.

Although constructive fraudulent intent can be inferred from the circumstances surrounding a transfer, in this case, the Debtor and the Debtor's Mother testified that the 2003 Conveyance was made as part of the Debtor's financial rehabilitation efforts. Both the nature of the Debtor's financial condition around the time of the 2003 Conveyance and the timing of the transfer support that assertion.

The undisputed testimony of the Debtor and the Debtor's Mother establish that prior to the 2003 Conveyance, the Debtor was attempting to recover from the financial difficulties associated with a separation from her husband. The Debtor testified that the Defendants paid the property taxes on the Parcel because, unbeknownst to the Debtor, her estranged husband had not been making the tax payments and she did not have the means to pay the taxes after they separated. Furthermore, the Debtor and the Debtor's Mother testified that the Debtor entered into the Sunapee Loan in order to consolidate her debts and lower her monthly payments. They also testified that the Defendants pledged their joint passbook savings account so as to allow the Debtor to qualify for a lower interest rate. Finally, the Debtor lacked the means to build a home on the Parcel, which was part of the understanding between the Debtor and the Defendants when they transferred the Parcel to her without consideration in 1999. The evidence establishes that, although the Parcel was an asset of the Debtor, it provided her with no liquidity or ability to meet her obligations as they became due. In fact, the annual real estate taxes on the Parcel was an additional burden on the Debtor's cash flow.

The timing of the 2003 Conveyance also militates against a finding of constructive fraud. First, the near contemporaneous nature of the 2003 Conveyance with the inception of the Sunapee Loan supports the Debtor's testimony that she entered into both transactions as part of a concerted effort to reduce her required cash outlay and to enable her to meet her obligations as they became due. The fact that the Bank is the only creditor that filed a claim in the Debtor's bankruptcy case indicates the Debtor did not incur significant debt after the 2003 Conveyance, which is consistent with her statement that the 2003 Conveyance was part of an effort to achieve financial rehabilitation. Second, the record indicates the 2003 Conveyance took place just shy of two years before the Debtor filed for bankruptcy protection, which demonstrates the Debtor's attempts to recover financially were successful for an extended period of time. The fact the Debtor ultimately failed to achieve a recovery and needed to file for bankruptcy protection is not enough to establish that the Debtor had reason to believe she was incurring debts beyond her ability to pay at the time of the 2003 Conveyance. The Court notes that the claim of the Bank is secured by the Defendants' joint passbook savings account, not by property of the estate. Accordingly, the claim will be paid in full.

In this case, the evidence fails to establish that the Debtor intended to incur, or believed or reasonably should have believed that she would incur, debts beyond her ability to pay as they became due. To the contrary, the Debtor intended the Sunapee Loan and the 2003 Conveyance to enable her to pay her debts as they became due. Accordingly, the Court finds the Trustee has failed to establish, by a preponderance of the evidence, that the transfer was constructively fraudulent under NH RSA 545-A:4(I)(b)(2).

V. CONCLUSION

For the reasons set forth in this opinion, the relief sought by the Trustee under Count II of the Complaint is denied. This opinion constitutes the Court's findings of fact and conclusions of law in accordance with Federal Rule of Bankruptcy Procedure 7052. The Court will issue a separate judgment in favor of the Defendants.

ENTERED at Manchester, New Hampshire.

Date: May 9, 2006

/s/ J. Michael Deasy
J. Michael Deasy
Bankruptcy Judge